CERTIFICATE.

SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1904.

No. 116.

GUILFORD B. KEPPEL, TRUSTEE, &c.,

vs.

TIFFIN SAVINGS BANK.

ON A CERTIFICATE FROM THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT.

FILED SEPTEMBER 17, 1903.

(19,069.)

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JUDD & DETWEILER, PRINTERS, WASHINGTON, D. C., JULY 11, 1904.

1 United States Circuit Court of Appeals, Sixth Circuit.

GUILFORD B. KEPPEL, Trustee, etc., Appellant, vs. TIFFIN SAVINGS BANK, Appellee.	)	No. 1177. Appeal from the District Court of the United States for the Northern District of Ohio.

Before Lurton and Severens, circuit judges, and Wanty, district judge.

This is an appeal from a judgment of the district court sitting in bankruptcy for the northern district of Ohio, allowing three claims filed against the estate of one Charles A. Goetz, a bankrupt, by the Tiffin Savings Bank.

From the transcript of the record it appears:

1. That Charles A. Goetz was upon his own petition adjudged a bankrupt October 12, 1900, and that the appellant Geo. B. Keppel was duly appointed trustee of the estate of the said bankrupt.

2. On September 17, 1901, the Tiffin Savings Bank filed for allowance four certain claims against the bankrupt's estate, to wit:

One note for $4,000.00 dated November 1, 1897.

One note for $2,000.00 dated October 9, 1900.

One note for $880.00 dated October 9, 1900.

One note for $35.00 dated October 11, 1900.

3. This note for $4,000.00 was secured by a real estate mortgage made in good faith more than four months before bankrupt's adjudication.

4. The note for $2,000.00 was made for a pre-existing debt and was secured by a mortgage of even date upon a second piece of real estate, the mortgagor being then insolvent and having an intent to prefer the said Tiffin Savings Bank.

5. Neither of the other notes were secured.

6. The trustee instituted suit in an Ohio court of common
2 pleas against the said Tiffin Savings Bank to recover as a part of the estate of the bankrupt the two parcels of real estate included within the two mortgages above mentioned and to have the mortgages aforesaid cancelled as null and void.

7. The said Tiffin Savings Bank defended and asserted the validity of both securities, and by its cross-petition sought to have same enforced.

8. The first cause of action was upon the mortgage made to secure the note for $4,000.00 and was decided against the trustee, and a decree enforcing the mortgage was pronounced upon the cross-petition of the mortgagee.

9. The said court of common pleas found in favor of the trustee upon his second cause of action finding the mortgage was made within four months of the mortgagor's adjudication as a bankrupt

and that it was made to secure a pre-existing debt and with a design to prefer the said Tiffin Savings Bank. It was, therefore, adjudged by the said common pleas court that said mortgage be annulled.

10. From the judgment and decree as an entirety the plaintiff appealed to the circuit court of Seneca county, Ohio, and perfected his appeal.

11. Upon the trial in the circuit court judgment was again given against the plaintiff upon his first cause of action and for the plaintiff upon the second cause of action. This judgment has not been reversed or annulled and remains undisturbed.

12. When the claims of the Tiffin Savings Bank were filed for allowance objection was made to the allowance of any one of them upon the ground that the said bank had not surrendered the preference resulting from the two mortgages to secure the two larger notes.

13. The claim for $4,000.00 was satisfied by the proceeds of the sale of the property mortgaged to secure that debt, and the question of its allowance as a claim against the bankrupt's estate consequently never came on for decision.

14. Only the trustee appealed from the judgment of the common pleas court, but that appeal took up the whole case which was retried in the circuit court upon the same pleadings and upon such evidence as the parties produced. There was evidence tending to show, that upon the retrial of the case in the said circuit court that the attorney representing the Tiffin Savings Bank announced to the court that the bank did not and could not maintain the preference secured by the mortgage to secure the $2,000.00, and that it
3 waived any preference thereunder. There was also evidence tending to show that although the bank declined any contention for the preference under the $2,000.00, its attorney refused to consent to judgment in favor of the trustee lest it might "prejudice its claim to dividends."

15. When the claims in question came on for allowance the referee ruled that the preference resulting from the $2,000.00 not having been "voluntarily surrendered" operated to prevent allowance of any claim whatever in favor of the said Tiffin Savings Bank and disallowed each of the three claims in question. Upon petition for review, Judge Wing, the district judge, reversed the referee, holding that the resistance interposed in the State court to the suit of the trustee to deprive the bank of its $2,000.00, did not operate to prevent the allowance of its claims.

16. Upon this state of facts this court desires the instruction of the Supreme Court that it may properly decide the questions of law thus arising and accordingly directs that the following questions be certified:

First. Can a creditor of a bankrupt, who has received a merely voidable preference, and who has in good faith retained such prefer-

ence until deprived thereof by the judgment of a court upon a suit of the trustee, thereafter prove the debt so voidably preferred?

Second. Upon the issue as to the allowance of the bank's claims was it competent, in explanation of the judgment of the Ohio circuit court in favor of the trustee and against the bank in respect of its $2,000.00 mortgage, to show the disclaimer made in open court by the attorney, representing the bank of any claim of preference, and the grounds upon which the bank declined to consent to a judgment in favor of the trustee?

Third. If the failure to "voluntarily" surrender the mortgage given to secure the $2,000.00 note operates to prevent the allowance of that note, does the penalty extend to and require the disallowance of both the other claims?

July 22, A. D. 1903.

HORACE H. LURTON,
Circuit Judge.
HENRY F. SEVERENS,
Circuit Judge,
GEO. P. WANTY, *Dist. Judge,*
Judges of the U. S. Circuit Court of Appeals for the Sixth Circuit.

4 United States Circuit Court of Appeals for the Sixth Circuit.

UNITED STATES OF AMERICA, *Sixth Judicial Circuit,* } ss:

I, Frank O. Loveland, clerk of the United States circuit court of appeals for the sixth circuit, do hereby certify that the foregoing certificate and statement of facts in the case of Guilford B. Keppel trustee etc. — Tiffin Savings Bank was duly filed and entered of record in my office by order of said court, and as directed by said court, the said certificate is by me forwarded to the Supreme Court of the United States for its action thereon.

In testimony whereof, I have hereunto subscribed my name, and affixed the seal of said court, at the city of Cincinnati, Ohio, this 7th day of Aug. A. D. 1903.

[Seal United States Circuit Court of Appeals, Sixth Circuit.]

FRANK O. LOVELAND,
Clerk of United States Circuit Court of Appeals for the Sixth Circuit.

[Endorsed:] United States circuit court of appeals for the sixth circuit. Guilford B. Keppel trustee *v.* Tiffin Savings Bank. Questions certified to the Supreme Court of the United States.

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JAMES H. McKENNEY
Clerk

Supreme Court of the United States,

OCTOBER TERM, 1904.

NO. 116.

GUILFORD B. KEPPEL, TRUSTEE, Etc.,

vs.

TIFFIN SAVINGS BANK.

BRIEF FOR TRUSTEE.

HENRY WELLER and
BUNN & ROYER,
Attorneys for Plaintiff.

ADVERTISER, TIFFIN, OHIO.

Supreme Court of the United States,

OCTOBER TERM, 1904.

NO. 116.

GUILFORD B. KEPPEL, TRUSTEE, Etc.,

vs.

TIFFIN SAVINGS BANK.

BRIEF FOR TRUSTEE.

This cause comes into this Court upon the certificate of the Circuit Court of Appeals for the Sixth Circuit.

The facts are stated and instructions are asked on three questions. We will consider these questions in their order.

> "First: Can a creditor of a bankrupt, who has received a merely voidable preference, and who has in good faith retained such preference until deprived thereof by the judgment of a Court upon a suit of the trustee, thereafter prove the debt so voidably preferred?"

The answer to this question is found in paragraph g, section 57, of the present Bankrupt Act. The language of this

paragraph at the time the question arose in this cause was as follows:

"The claims of creditors who have received preferences shall not be allowed unless such creditors shall surrender their preferences."

What is the meaning of this provision — when and how must a creditor surrender his preference in order that his claim or claims may be allowed?

Our contention is that the surrender must in all cases be voluntary and must, therefore, be made before any Court has, by its judgment, avoided the preference.

It is true that the word, surrender, is used with widely different meanings. A general surrenders his army under pressure when he can fight no longer, or when to continue the fight would mean the complete annihilation of his soldiers. But this is not the primary meaning of the word. It is to render over: "To give back; render again; restore." (Century Dictionary). In law the term has had a technical meaning since the days of Littleton, and was used in conveying "an estate for life or years to him who has an immediate estate in reversion or remainer," (Bouvier). These meanings imply a voluntary act.

That Congress intended a voluntary surrender, we think, will appear quite clearly from a history of legislation and judicial construction on this point.

The Bankrupt Act of 1867, as originally passed, had this provision in section 23: "Any person who, after the approval of this act, shall have accepted any preference, having reasonable cause to believe that the same was made or given by the debtor, contrary to any provision of this act, shall not prove the debt or claim on account of which the preference was made or given, nor shall he receive any dividend therefrom until he shall first have surrendered to the assignee all property, money, benefit, or advantage received by him under such preference." * * * * 14 Statutes at Large, 517.

By the amendment of 1874, the foregoing provision ap-

pears to have been repealed (section 21) and in its stead was provided that a person who has received a preference, "if a creditor, shall not in case of actual fraud on his part, be allowed to prove more than a moiety of his debt;" 18 Statutes at Large, p 178.

It is not very clear what became of this amendment, for in the Revised Statutes of 1878 the original provision, with some necessary verbal changes, again appears as section 5084.

Compared with these provisions of the former bankrupt law, paragraph g, section 57, of the present act is certainly clear and explicit. Plurals are used instead of singulars, and for the word "until" (a limitation as to time only) the word "unless" (a limitation as to choice or election) is substituted.

By omitting from the present law the amendment of 1874, and all provisions similar thereto, and adopting language stronger and clearer than the surrender clause of the original act of 1867, Congress must have intended a construction not less severe than that given to such original act prior to its amendment.

We therefore call the Court's attention to the following cases in which the surrender clause of the Act of 1867, prior to its amendment, was construed:

In re Lee, No. 8179 Fed. Cases, s. c. 14 N. B. R. 89.
In re Richter, No. 11,803, Fed. Cases, s. c. 1 Dill. 544.
In re Leland, No. 8,230, Fed. Cases, s. c. 7 Ben. 156.
In re Stephens, No. 13,305 Fed. Cases, s. c. 3 Biss. 137.
In re Drummond, 4094 Fed. Cases, s. c. 4 Biss 149.
In re Graves, 9 Fed. Rep. 816.

For the convenience of this Court, we will here give some extracts from these cases. We do this the more cheerfully because the Judges quoted, though not sitting as Courts of last resort, bear honored names in our jurisprudence:

IN RE RICHTER ESTATE.

Decided in 1870 by Judge Dillon.

> "1. Where an assignee brings his action under the 35th section of the bankrupt act (of 1867 (14 Stat. 534)) to recover of a creditor of the bankrupt property alleged to have been sold or conveyed to him in fraud of the act, and where the defendant in such action denies his liability, resists a recovery, goes to trial, and judgment passes against him, such a judgment conclusively establishes that the creditor sought to obtain a fraudulent preference. Payment of such a judgment under execution issued is not such a surrender as is contemplated by section 23 of the act, and will not entitle the party to prove up the claim, in satisfaction of which he received property from the bankrupt by way of illegal preference."

In his opinion in this case Judge Dillon says, among other things: "The cardinal idea of the bankrupt act is an indiscriminating distribution of all the effects of the debtor, to all of his creditors. This legislation is essentially founded upon the doctrine that equality is equity. When a debtor finds himself embarrassed, experience has shown that there arises in his mind a strong temptation, either to conceal his property, or to distribute it as his favor or his enmity, or both may dictate. * * * * The temptation to prefer, and the danger of doing so, inhere in the situation of an insolvent debtor; and hence it is (to use language applied to purchases of trust property by trustees) 'the wise policy of the law has put the sting of a disability into the temptation, as a defensive weapon against the strength of the danger

which lies in the situation.' Notes to Fox vs. Mackreth 1 Lead Cas. Eq. 161."

"The 18th, 23rd, 29th, 35th, and 39th sections of the bankrupt act abundantly evince the anxiety of the Legislature to guard against preferences, which operate as a fraud upon the policy of the act. Such preferences are not only prohibited and declared void, but certain penalties are denounced against creditors who, under the circumstances specified, accept of preferences."

"So that the bankrupt act says decisively to every person who, under the circumstances specified, has received a preference: 'Surrender what you have received and you shall lose nothing. If you refuse, and the assignee recovers the property or its value you shall get nothing. Make your election.'"

IN RE STEPHENS ESTATE.

Decided in 1872 by Judge Hopkins.

> "1. A full surrender of a creditor of a preference fraudulent under the act restores him to all his rights, and he may prove his claim against the estate."
>
> "2. Whether this may be done after suit is brought, is a matter of discretion with the court. It will not be allowed after a recovery."

We also quote the following from the opinion: "The preference is what the law denounces, the intent of the act being to secure an equal distribution of the estate of a bankrupt among all his creditors; and if a creditor voluntarily yields a preference he may have acquired or attempted to acquire, and surrenders all the property, so that it does not in any manner interrupt the equal distribution required by the act, the party is restored to his rights as they stood before the preference. If a creditor, having received preference, refuses

to surrender, and a suit is prosecuted against him by the assignee for the property or money unlawfully received as a preference, and a recovery is had against him, he cannot then surrender and receive the benefits of that section."

"A party should not be allowed to experiment and speculate upon the ability of the assignee to prove a case against him, and when he sees he has succeeded then to plead guilty and surrender, and take the benefit of section 23. Such a practice ought not to be tolerated."

IN RE LELAND ESTATE.

Decided in 1874 by Judge Blatchford.

> "This provision of the 39th section is to be construed in connection and in harmony with the provision of the 23rd section; and there cannot be such a surrender by the creditor, as is spoken of in the 23rd section, after there has been a recovery of the property by the assignee under the 39th section, or under the 35th section."

We also quote the following from the opinion:

"If, under the 23rd section, the preferred creditor were allowed to surrender to the assignee the property received in preference, even after it has been recovered back by the assignee as mentioned in the 39th section, so as to be able to prove his debt, no creditor taking a preference could ever be debarred from proving his debt. If, under the 39th section, it were held that the mere taking of a preference by a creditor would debar him from proving his debt, without the precedent necessity for a recovery back by the assignee of the property conveyed in preference, there never could be any scope for the operation of the 23rd section in respect to a surrender. The interpretation heretofore given by this court to these provisions of the 23rd and 39th sections has

been (in re Davidson (Case, No. 3,599)) that the clause in the 39th section, in respect to not allowing the creditor to prove his debt in bankruptcy, applies only to cases in which the assignee is compelled to resort to legal proceedings to recover the property transferred in violation of the act; that the creditor who claims to retain the property makes himself conclusively a party to the fraud against the act, by resisting the claim of the assignee to recover the property in case the assignee is successful; but that, where the creditor avails himself of the locus poenitentiae given to him by the 23rd section, by voluntarily surrendering the property to the assignee, he ceases to be a party to the fraud, and may prove his debt in bankruptcy and receive dividends on it. This view is concurred in by Judge Longyear, in re Scott (Case No. 12,518), and in re Kipp (Id. 7,836); by Judge Deady, in re Walton (Cases Nos. 17,128, 17,130); by Judge Hopkins, in re Stephens (Case No. 13,365); and by Judge Dillon, in re Richter (Id. 11,803)."

IN RE LEE ESTATE.

Decided in 1876 by Judge Wallace.

> "2. Under the prior law a preferred creditor who did not surrender his preference until he was compelled to do so by the judgment of a court, could not prove his debt."

We also quote the following from the opinion:

"Second. Treating the case as one to be determined by the law in force prior to the amendments, the creditor who has not surrendered a preference until he has been compelled, after contest, to do so by the judgment of the court, is precluded from proving the debt upon which the preferential payment was received. I have held repeatedly that under the terms of the 23rd section of the act, prior to the amendment,

a voluntary surrender was a pre-requisite to the right to prove, and that it was too late for the creditor to avail himself of the privilege after he had elected to contest the assignee's title to the money or property preferentially received. Whether the action of the creditor was in actual fraud of the act, or only a constructive fraud upon it, he is chargeable with knowledge of its illegality, and must be assumed to have made his election with such knowledge."

We might quote from other cases to the same effect; but the foregoing, we think, are sufficient to remind this Court of the construction given to the surrender clause of the former bankrupt law. While some of the judges allowed a surrender pending litigation, we find no case where a creditor was allowed to surrender his preference after judgment against him, and thus save his right to have his claim allowed.

This question under the present act has been before the Court in the following cases:

In Re Richard, 94 Fed. Rep., 633.
In Re Owings, 109 Fed. Rep., 624.
In Re Keller, 109 Fed. Rep., 162.
In Re Greth, 112 Fed. Rep., 978.

The last three of these cases follow the decisions under the former law, and in the first the facts were so different that the reasoning of the court is scarcely applicable to the question now before the Court.

In Re Greth, which is the latest case on this subject we have been able to find, Judge McPherson reviews the authorities at some length and comes to the conclusion that the surrender by the claimant must be voluntary; that after contesting the validity of his preference to final judgment he cannot then surrender because he no longer has anything to surrender, having been unwillingly deprived of the same.

It has been said that this is a "harsh rule in case the creditor has acted in good faith, without actual fraud on his

part." But the courts have nothing to do with the harshness of the rule, except as the same may assist us in arriving at the intention of the legislature.

The intention of Congress, however, to establish a "harsh rule," if such it must be called, is conclusively demonstrated, we think, by adopting paragraph g, section 57, having in mind the construction given to the act of 1867 prior to the amendment of 1874. Besides, the reasoning of such eminent Judges as Dillon, Blatchford and Wallace, in the decisions already quoted, not only gives the reason for the rule, but amply justify its wisdom.

> "Second: Upon the issue as to the allowance of the bank's claims was it competent, in explanation of the judgment of the Ohio Circuit Court in favor of the trustee and against the bank in respect of its $2,000.00 mortgage, to show the disclaimer made in open court by the attorney, representing the bank, of any claim of preference, and the grounds upon which the bank declined to consent to a judgment in favor of the trustee?"

In the action of the trustee against the Tiffin Savings Bank to avoid the mortgages there were two causes of action — one to avoid the $4,000.00 mortgage and the other to avoid the $2,000.00 mortgage. In the Court of Common Pleas the Bank was successful on the first cause and the trustee on the second cause. The Bank did not appeal, but the trustee did. Under the statutes of Ohio (section 5225) an appeal takes up the whole case, and it is tried de novo, in form at least, in the appellate court. The trustee had no desire to appeal from the judgment of the Common Pleas Court on the $2,000.00 mortgage, because on that he had

been successful. But under the statutes he could not separate the two causes of action at that stage of the litigation and appeal from only one cause. He could in the first place have brought two action — one on each mortgage. An appeal then in either case would have left the judgment in the other case undisturbed. Can it be claimed then that because the trustee brought one action instead of two, in order to save costs, that that fact gave the Bank one more chance to surrender?

It is true that the appeal vacated the judgment; but if the Bank then surrendered its preference on the $2,000.00 claim, it did so nevertheless because the judgment of the Common Pleas Court was against it and did not do so voluntarily. In the language of Judge Hopkins in the Stephens case, from which we have already quoted: "A party should not be allowed to experiment and speculate upon the ability of the assignee to prove a case against him. * * * * And if on examination, I should conclude I had the power to prevent it, I shall expect a party to elect, and having elected, shall hold him to his election."

There is another and equally important consideration in answering the second question. The record of the case in the Circuit Court shows that there was a trial and that a judgment was rendered against the Bank annulling the $2,000.00 mortgage. This judgment operated on the particular real estate in question, and was therefore a judgment in rem and conclusive whenever and wherever the fact of such judgment was in controversy. The finding and judgment further furnish conclusive evidence that the validity of the $2,000.00 mortgage was tried and decided. Evidence that the Bank abandoned its claim to this mortgage at the trial would contradict the record. There is no uncertainty as to what issue was decided and therefore no occasion for parol evidence to show the facts.

The principles here applied are so well settled that we need not cite authorities.

We claim then that the evidence of what was said by attorneys at the trial was irrevelant because it was then too late for the Bank to surrender its preference; that in any event it did not amount to a surrender; and that it was incompetent because it contradicts the record.

> "Third: If the failure to 'voluntarily' surrender the mortgage given to secure the $2,000.00 note operates to prevent the allowance of that note, does the penalty extend to and require the disallowance of both the other claims?"

This question has been answered in the affirmative by the Circuit Court of Appeals for the Eighth Circuit, in the case of Swartz vs. Fourth Nat. Bank, 117 Fed. Rep., 1.

At page 5 of the report, the Court, after quoting section 57g of the bankrupt law, say:

"The unequivocal language and the unquestionable legal effect of this section are to prohibit the allowance of any claim of a creditor who has received a preference, either upon that or upon any other claim he holds against the estate of the bankrupt, unless he has first surrendered his preference."

It seems to us that virtually the same question was decided in the same way by this Court in the case of

Perie, et al. vs. Chicago T. & T. Co. 21 S. C. Rep., 906.

The second syllibus of that case is as follows:

> "2. A creditor who has received payments of money from an insolvent debtor within four months before petition in bankruptcy was filed for the debtor, but who did not know or have reasonable cause to believe

> that the payments were intended to give him a preference, the debtor not intending to give a preference, cannot be compelled, under the bankruptcy act, 60b, to repay the money to the trustee in bankruptcy, **but under 57g he must surrender the preference that he has received, before any claim by him against the estate can be allowed.**"

The object of the bankrupt law is to secure the equal distribution of the bankrupt's estate among his creditors, so far as it can be done. The Savings Bank had three claims against Goetz all belonging to the same class. It received a voidable preference, by way of mortgage security, on one of them which it refused to surrender, and it thereby forfeited its right to have any of its claims allowed. The case stands just as though the three claims had been united into one and a mortgage given to secure $2,835.00, instead of $2,000.00.

Respectfully submitted,

HENRY WELLER and
BUNN & ROYER,
Attorneys for Plaintiff.

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JAMES H. McKENNEY,
Clerk.

Supreme Court of the United States.

October Term, 1904.

GUILFORD B. KEPPEL, TRUSTEE, ETC.,
vs.
TIFFIN SAVINGS BANK.
No. 116.

Brief for the Tiffin Savings Bank.

GEORGE E. SENEY,
MILTON SAYLER,
JOHN L. LOTT,
for the Savings Bank.

Supreme Court of the United States.

October Term, 1904.

GUILFORD B. KEPPEL, TRUSTEE, ETC.,
vs.
TIFFIN SAVINGS BANK.
No. 116.

Brief for the Tiffin Savings Bank.

Three questions are certified to this court by the Circuit Court of Appeals for decision. They involve the construction to be placed upon the word "preferences" in paragraph "*g*," section 57 of the act of July 1, 1898, (30 Stat. 554, 560,) commonly called the Bankrupt Act. That paragraph reads as follows:

> The claims of creditors who have received *preferences* shall not be allowed unless such creditors shall surrender their preferences.

The pertinent facts are these:

Immediately after Goetz was adjudged a bankrupt, a trustee was appointed, who brought suit in the Court of Common Pleas of Seneca County, Ohio, (the bankrupt being a citizen of that county,) to have declared void the two mortgages given by Goetz to the Savings Bank. Both courts in which the case was tried held in favor of the bank as to the $4,000 mortgage, but against it as the $2,000 mortgage.

When the bank presented its three notes for allowance, the referee refused to permit the bank to make proof as to any of them, for the reason that it had not made a *vol-*

untary surrender of its mortgage given to secure its $2,000 note. The failure to do so, he contended, precluded the allowance of any claim the bank held against the bankrupt. The District Court reversed the action of the trustee and permitted the bank to prove its claims; the trustee took an appeal to the Circuit Court of Appeals, and that court certifies the questions here for decision.

The trustee instituted his suit in accordance with the provisions of sections 6343 and 6344, Revised Statutes of Ohio, as amended April 26, 1898. (93 Ohio Laws, 290.) Section 6343, among other things, provides:

> And every such sale, conveyance, transfer, mortgage or assignment made, * * * by any debtor or debtors, in the event of a deed of assignment being filed within ninety (90) days after the giving or doing of such thing or act, shall be *conclusively* deemed and held to be fraudulent, and shall be held to be void as to the assignee of such debtor or debtors, where upon proof shown, such debtor or debtors were actually insolvent at the time of the giving or doing of such act or thing, whether he or they had knowledge of such insolvency or not. * * *

By section 6344 it is further provided:

> Any creditor or creditors, as to whom any of the acts or things prohibited in the preceding section are void, * * * may commence an action in a court of competent jurisdiction to have such acts or things declared void, and such court shall appoint a trustee according to the provisions of this chapter, who upon being duly qualified shall proceed by due course of law to recover possession of all property so sold, conveyed, transferred, mortgaged or assigned, and to administer the same for the equal benefit of all creditors. * * *

In connection with these Ohio statutes it is proper to call attention to that provision of paragraph "*e*," of section 67 of the Bankrupt Act, which reads as follows:

> And all conveyances, transfers, or incumbrances of his property made by a debtor at any time within

four months prior to the filing of the petition against him, and while insolvent, which are held null and void as against the creditors of such debtor by the laws of the State, Territory, or District in which such property is situate, shall be deemed null and void under this act against the creditors of such debtor if he be adjudged a bankrupt, and such property shall pass to the assignee and be by him reclaimed and recovered for the benefit of the creditors of the bankrupt.

I.

The First Question.

Can a creditor of a bankrupt, who has received a merely voidable preference and who has in good faith retained such preference until deprived thereof by the judgment of a court upon a suit of the trustee, thereafter prove the debt so voidably preferred?

The mortgage having been given by Goetz while insolvent, and within four months of the filing of his petition in bankruptcy, by operation of law alone became absolutely void, and the bank had no preference whatever.

(*a.*) The bank claims that it had no preference whatever within the meaning of the statute. The Ohio law declares that a mortgage to secure a pre-existing debt, given within ninety days of the making of an assignment, "shall be *conclusively* deemed and held to be fraudulent," and shall be held to be void where, upon proof shown, the mortgagor was insolvent at the time of giving the mortgage, whether the mortgagee had knowledge of such insolvency or not. As to such a mortgage, so given, the only question to be determined is whether, at the time of giving, the mortgagor was insolvent. If so, upon a proper determination of that fact, the mortgage at once, *by force of the statute alone*, becomes absolutely void, and no decree of a court can make it more so.

The same thing is true under section 67 of the Bankrupt Act. A mortgage given within four months prior

to going into bankruptcy, if at the time of the giving the mortgagor be insolvent, by force of that section and of the Ohio statute above cited, becomes absolutely void. It becomes void by operation of law, and before any court can act upon it.

Now in the face of these express enactments, what necessity was there for the bringing of a suit to cancel a mortgage which the law already had pronounced dead? The suit was brought to cancel the $4,500 mortgage given some three years before the act of bankruptcy, and which the courts held to be good. This second mortgage was included in the suit, we presume, to have a second pronouncement of the death sentence; or, perhaps, with an idea on the part of the trustee of inflicting punishment after death.

Goetz having been adjudged a bankrupt, and the law having declared the mortgage void if given while Goetz was insolvent, what fact was there about which to contest? Only one; the question of the insolvency of Goetz at the time he gave the mortgage. The burden of showing that fact was upon the trustee. (*In re Chappell*, 113 Fed. Rep. 545.) It is not claimed that the debt is not a *bona fide* one, or that the bank knew at the time that Goetz was insolvent. The bank, therefore, was entitled to a determination of the question whether Goetz was insolvent at the time he gave this mortgage; for if he was not, the mortgage was good, and it could not be said that the giving of the mortgage constituted a preference in any view of the law.

What did the bank really have? Nothing with life or vitality after the act of bankruptcy and after the finding of a state of insolvency at the time of giving the mortgage. The bank had a dead mortgage; to use a common expression, it had "a chicken dead in the shell." It had neither title to, nor possession of, any property of the bankrupt; nor had it any right under the mortgage that

it could enforce, by any sort of proceeding, against either the bankrupt or his creditors.

The mortgage was given three days before the filing of the petition in bankruptcy. The certificate does not disclose when the note, which the mortgage purported to secure, became due. We may fairly presume, therefore, that the note had not become due at the time of the filing of the petition. The note not being due at that time, the bank had neither the title to, nor the possession of, the property described in the mortgage; for under the law of Ohio the title and possession both remain in the mortgagor until the condition in the mortgage is broken. As said in the case of *Lessee of Ely* v. *McGuire*, 2 Ohio, 372:

> The title of mortgaged premises remains in the mortgagor as against all the world, except the mortgagee, and also as against him until it becomes absolute at law, by the non-performance of the condition, and the mortgagee takes legal steps to reduce the premises to possession.

And this rule was again stated in *Bradfield* v. *Hale*, 67 Ohio St. 316, 323.

While in one sense this mortgage may have been a conditional conveyance—a conveyance upon the happening of a certain condition—it never took effect so as to convey, or transfer anything, because the law stepped in and rendered void the instrument before the condition upon which the conveyance was to take place happened. In a general sense, however, in Ohio a mortgage is merely a security for a debt. Thus in *Harkrader* v. *Leiby*, 4 Ohio St. 602, it is said, page 612:

> A mortgage is now treated in both courts (of law and equity) as a mere security for the debt.

Again, in *Sun Fire Office* v. *Clark*, 53 Ohio St. 414, it is said, page 424:

> A mortgage being a mere security for a debt, is extinguished by its payment without any reconvey-

> ance. The mortgage of itself does not make the mortgagee a freeholder, and a judgment recovered against him does not become a lien on the land, nor is it liable to the dower rights of his wife. It has *none of the incidents* of a legal or equitable title.

In *Kernohan* v. *Manss*, 53 Ohio St. 116, speaking of the nature of a mortgage, the court says, page 133:

> Where a promissory note is secured by mortgage, the note, not the mortgage, represents the debt. The mortgage is, therefore, a mere incident of the debt. * * * Being but an incident of the debt, the mortgage remains, until foreclosure or possession taken, in the nature of a *chose in action*. Where given to secure notes it has no determinative value apart from the notes, and, as distinct from them, is not a valid subject of assignment.

Being in the nature of a chose in action, it could not be enforced without action; and it could not be enforced by action, because the statute expressly declared it a nullity.

The trial court having found that at the time of giving the mortgage Goetz was insolvent, (the bank being entitled to have that fact judicially declared before conceding its mortgage to be void,) took no appeal from that finding. Having decided in favor of the bank as to the $4,000 mortgage, the trustee took an appeal to the Circuit Court. That appeal vacated the decree of the Common Pleas Court and took up the whole case for retrial in the Appellate Court. (*Teaff* v. *Hewitt*, 1 Ohio St. 511: *Bassett* v. *Daniels*, 10 Ohio St. 617, 618.) The bank took no appeal and made no claim in behalf of the mortgage in the Circuit Court, its attorneys expressly stating upon the trial that they made no claim of preference under the mortgage. They, therefore, waived any claim to a preference before any final decree was entered against them. The proceeding being equitable in its nature, the case went up on appeal; the whole case was tried anew. There was, therefore, no affirmance of a judgment of the

lower court, but the entering of a decree entirely independent of the decree of the Common Pleas which had been vacated by the appeal.

(*b.*) Having discussed the nature and effect of this mortgage, and of the proceeding to cancel it, we come to the question whether the giving of this mortgage constituted a *transfer* of property within the meaning of section 60, paragraph "*a*," of the Bankrupt Act, as defined in section 1, definition 25, of that act, to wit:

> "Transfer" shall include the sale and every other and different mode of *disposing of or parting with property or the possession of property*, absolutely or conditionally, as a payment, pledge, mortgage, gift, or security.

It must be borne in mind that under this definition it is the disposing of or parting with property, or the possession of property, that constitutes a transfer. Tested in the light of the Ohio decisions, it can hardly be said that this mortgage did any one of the things embraced within the definition. By this mortgage Goetz did not dispose of (that is, alienate) or part with the property, or the possession of the property. The act was not a completed act and would not be until condition broken. The mortgagee acquired nothing under the mortgage until the condition was broken. Before that right attached, the law stepped in and declared the instrument void.

It may be that in some States a mortgage of this character may be regarded as of such a nature as to constitute a preference, but as this case arose in Ohio the question must be determined with reference to its nature there, as declared by the Ohio decisions; and the question of preference decided by considering the effect the Ohio statutes had upon this instrument.

(*c.*) Coming to the Federal decisions, we find a contrariety of opinion as to what constitutes a preference and as to when it shall be surrendered in order to entitle the person holding it to prove his claims. As to the cases cited

in the brief of opposing counsel, it is sufficient to say that most of them arose under the act of 1867, and were cases in which there had been an actual payment of money, or the actual receipt or possession of property, or where the person had been a party to an actual fraud, and cannot be held controlling here. Most of the cases bearing upon the preference clause under the present law may be found in the notes in 1 Fed. Stat. Annotated, pp. 664, 665, to which the court is referred.

In the case at bar, in reversing the action of the trustee in refusing to permit the bank to prove its claims, Judge Wing, speaking with respect to the rights the bank acquired under the mortgage, says:

> It (the bank) had a fancied right which it sought to enforce, but in fact had no rights in the mortgage whatever. The mortgage was absolutely void, both under the Bankrupt Act and the State law, and was so decreed by the State courts.

In the case of *Pirie* v. *Trust Co.*, 182 U. S. 438, the question was whether a payment of money was a transfer of property within the meaning of the law. The court held it to be a transfer because it was the giving or conveying of something of value. There, however, there was an actual payment and delivery of property— a completed transaction—a passing of property.

In *Bank* v. *Massey*, 192 U. S. 138, this court, in defining what acts constitute a transfer, says, page 147:

> These transfers of property, amounting to preferences, *contemplate the parting with the bankrupt's property* for the benefit of the creditor and the consequent diminution of the bankrupt's estate. It is such transactions, operating to defeat the purposes of the act, which under its terms are preferences.

In this case there was no parting with property and no contemplation of parting with it. The fact that Goetz gave a mortgage which did not pass title or possession, rebuts the idea that he contemplated parting with his

property. Had a parting with the property been contemplated, it is fair to presume that a deed of some sort would have been given the bank by Goetz,

A brief reference to the cases cited by opposing counsel under the present law is appropriate.

In re Richard, 94 Fed. Rep. 633, was a case where certain judgments were obtained within four months of the filing of the petition in bankruptcy, upon which executions were sued out and levies made. It also appears some payments had been made thereon. In answer to the question whether the judgment creditors should be permitted to prove their claims after contest, the court says, page 637:

> There is no denial of respondents' "debt," as defined in section 1, nor allegations that there was any actual fraud in obtaining the judgments—only such fraud of the bankrupt law as vitiates any lien acquired. The debts are due. Respondents have received and can receive no preference, lien, or advantage by reason of or under the judgments of the magistrate's court. *They are nullities* in this court to this extent. * * * Respondents have attempted to gain an advantage and failed. These proceedings as far as gaining a lien, are void. The respondents must * * * refund what has been collected under these proceedings. They are still creditors of the bankrupt, after a fruitless fight. They have gained no advantage and acquired no lien, but are still creditors unsecured. Should they be punished by a loss of their debts because they were vigilant? The law does not so provide. It favors vigilance, especially when untainted with fraud. * * * Respondents have received no preference and been parties to no actual fraud, but only to such fraud of the operation of the Bankrupt Act as vitiates their proceedings. They are creditors, and on a surrender of the amount collected of the bankrupt estate, are entitled to prove their claims as other unsecured creditors.

In re Owings, 109 Fed. Rep. 623, was a case where the creditor had accepted a stock of goods of the debtor in

satisfaction of a debt, within four months of the filing of a petition in bankruptcy, well knowing at the time the goods were taken that the debtor was insolvent. Upon suit brought to recover the value of the goods received, the creditor offered to return $900, claiming that to be their value. The trustee recovered a judgment for $1,400. The creditor was not allowed to prove his claim. But this was on the theory that from the beginning the creditor was a wrongdoer, and did not come into court with clean hands.

But that is not this case. It is not claimed, and the record does not show, that at the time of taking this mortgage the Savings Bank had any knowledge that Goetz was insolvent. In the absence of such a showing, the presumption is the bank had no such knowledge. *Bank* v. *Massey*, 192 U. S. bottom page 148.

All that was held in *In re Keller*, 109 Fed. Rep. 118, was, that a creditor who had received a payment on his claim within four months, the debtor at the time being insolvent, must return the payment before he could share in the distribution of the estate. The court points out (pp. 124, 125) that such a creditor has a choice of two things: either to return the payment and share in the distribution, or retain the payment and be denied the right to share in the proceeds.

In re Greth, 112 Fed. Rep. 978, holds, however, that where a judgment has been obtained within four months of the filing of a petition in bankruptcy, and the judgment creditor defends his judgment, he is not permitted to share in the proceeds, although he has never received anything upon the judgments. We fail to see the force of the reasoning in this case. What was there to contest? The judgments were rendered within four months of the beginning of proceedings in bankruptcy; the debtor had been adjudged a bankrupt; insolvent at the time of the taking of the judgments. The statute nullified the

judgments; there was nothing for the decree of a court to act upon, and a suit to declare void a judgment already by statute made void is a useless proceeding. It could not even be claimed that such a judgment would be a cloud upon the title of the property of the bankrupt, for it would be cancelled by operation of law.

Swarts v. *Bank*, 117 Fed. Rep. 1, was a case where a creditor had received a payment upon its claim within the prohibited time. The court held that the payment must be surrendered before the creditor could share in the distribution. Speaking of the rule for determining a preference, the court says, page 4:

> The test of a preference under the act is the *payment*, out of the bankrupt's property, of a larger percentage of the creditor's claim than other creditors of the same class receive.

Payment is made the test of a preference; and in the case at bar there was no payment. (As to payment see *Bank* v. *Gettinger*, 68 Ohio St. 400.)

In *In re Steam Vehicle Co.*, 121 Fed. Rep. 939, Judge McPherson (who delivered the opinion in *In re Greth*, *supra*) held that "*payment* means at least that value has passed in some form or other" from the bankrupt to the creditor.

Western Tie & Lumber Co. v. *Brown*, 129 Fed. Rep. 728, was a case where the bankrupt owed the company a large amount of money. In the course of their dealings and within four months of the time of going into bankruptcy it retained and credited upon its claims certain moneys due the bankrupt, which it had retained from amounts paid his workmen. The question whether the retention of this money and the applying it upon the claim created a preference was contested, not only before the referee and the District Court, but also in the Circuit Court of Appeals—all holding that it constituted a preference. The Court of Appeals points out that the test of a prefer-

ence is the transfer—the passage of the property of the debtor to the creditor. Notwithstanding the contest made by the company the latter court permitted it to prove its claim upon repayment to the trustee of the moneys retained by it.

We respectfully submit that, even if the bank had assigned this mortgage to the trustee, nothing would have been added to the estate, for it was not property, and would not have been a transfer of property. It was a thing which had neither life nor force, since the statute declared it to be *conclusively* void. The bank had received nothing of value from its debtor and had nothing to return. It should, therefore, be permitted to prove its claims before the trustee.

Again: The referee held that the bank had not made a *voluntary* surrender of its so-called preference, and therefore was not entitled to prove its claim. By so holding the referee read into the act something that is not there. The language of the act is *surrender*, not *voluntary surrender*. If a referee may inject into the act the word *voluntary*, it would be but a step further to require that a *willing*, a *cheerful* or even a *joyful* surrender be made. Webster defines *surrender* as the giving or delivering possession of anything upon *compulsion* or demand, and the same definition is to be found in the Standard and Century dictionaries. If the ruling of the referee be correct, then a creditor who, in good faith, has accepted a payment or security, without knowledge of the insolvency of his debtor, must blindly surrender that which he has received, without an opportunity for a determination of the question of insolvency at the time of the receiving of the payment or security, or of the question whether that which he has received constitutes a preference. The creditor is not required to submit to the ruling of the referee, but is entitled to the decision of the court upon the point. (Sec. 57, par. *f*.) If the contention of the referee be correct, then the mere submission of a question

to a court for decision deprives the creditor of a right to prove his claims. We submit the law does not so provide.

That the construction here contended for is the correct one is apparent from the fact that a *bona fide* creditor who, without knowledge of the insolvency, has received a preference, has the option of retaining his preference and not participating in the distribution of the fund, or surrendering his preference and participating. *In re Keller*, 109 Fed. Rep. 124, 125. This rule applies where the creditor has acted in good faith. And, as pointed out in the recent case of *Kaufman* v. *Treadway, Trustee*, (decided November 28, 1904,) Mr. Justice Brewer delivering the opinion, Congress did not extend the rule to creditors who knowingly participate in any fraud.

We submit that the bankrupt act aims to protect the equities of all creditors, and we do not believe such a construction should be placed upon it as will deprive the bank of its right to prove its just claims, in order to increase the dividends of other creditors of the same class, merely because the bank, in the suit to set aside its mortgage given three years before the act of bankruptcy (and in which the second mortgage was also included), which was held to be valid, insisted that it was entitled to a judicial determination of the question whether, upon the facts and the law, it being a *bona fide* creditor, and not a party to any fraud, its later mortgage did or did not amount to a preference.

II.

The Second Question.

Upon the issue as to the allowance of the bank's claims, was it competent, in explanation of the judgment of the Ohio Circuit Court in favor of the trustee and against the bank in respect of the $2,000.00 mortgage, to show the disclaimer made in open court by the attorney representing the bank of any claim

of preference, and the grounds upon which the bank declined to consent to a judgment in favor of the trustee?

Upon this point the certificate is silent as to the character of testimony offered to show the disclaimer made by the attorneys for the bank upon the trial of the case in the Circuit Court. In the absence of a showing of its nature, the presumption is that the proof offered (if proper proof could be offered for that purpose) was proper. We submit that (for the purpose of showing the waiver) it was competent to introduce the record of the case made in that court for the purpose of showing just what occurred upon the trial, and upon what the decree was based.

The laws of Ohio provide for the appointment of official stenographers. (Rev. Stat. 475 *et seq.*; 91 Ohio Laws, 688.) They are required to take an oath of office. When called upon to do so in any case, it is the duty of the official stenographer to take accurate shorthand notes of all the proceedings, "which notes shall be filed in the office of the official stenographer, and preserved." These notes, therefore, become a part of the official record in the case. If requested, it is the duty of the stenographer to extend his notes into longhand; otherwise he does not. Where such notes have not been extended, it would be entirely competent to call the stenographer, with his notes, to the witness stand, and have him read his notes upon such points as may be desired. It would have been perfectly competent, then, (there being an official stenographer of the Circuit Court of Seneca County,) to have called him to the witness stand, with his official notes, and have him read just what his notes showed with respect to the disclaimer made by the attorney for the bank in the Circuit Court. And as a matter of fact, this was what was done. Being part of the official record of the case, we submit such proof was competent, and should be so held.

III.

The Third Question.

> If the failure to "voluntarily" surrender the mortgage given to secure the $2,000.00 note operates to prevent the allowance of that note, does the penalty extend to and require the disallowance of both the other claims?

Upon this point the decisions are so conflicting that we cannot do better than to refer the court to the learned opinion of Judge Hammond in the case of *In re Wolf & Levy*, 122 Fed. Rep. 127, in which reference is made to the various decisions upon the point. (pp. 132–140.)

We respectfully submit that the first and second questions should be answered in the affirmative and the third in the negative.

GEORGE E. SENEY,
MILTON SAYLER,
JOHN L. LOTT,
for the Savings Bank.

DECEMBER 12, 1904.

Supreme Court of the United States.

No. 116.—October Term, 1904.

Guilford B. Keppel, Trustee, etc., vs. Tiffin Savings Bank. } On a certificate from the United States Circuit Court of Appeals for the Sixth Circuit.

[April 3, 1905.]

Charles A. Goetz became a voluntary bankrupt on October 12, 1900. George B. Keppel, the trustee, sued the Tiffin Savings Bank in an Ohio court to cancel two real estate mortgages executed by Goetz, one to secure a note for four and the other a note for two thousand dollars. The mortgage to secure the four thousand-dollar note was made more than four months before the adjudication in bankruptcy. The mortgage securing the two thousand-dollar note was executed a few days before the bankruptcy, the mortgagor being at the time insolvent and intending to prefer the bank. The bank defended the suit, averring its good faith and asserting the validity of both the securities. In a cross petition the enforcement of both mortgages was prayed. The court held the mortgage securing the four thousand-dollar note to be valid and the mortgage securing the two thousand-dollar note to be void. The trustee appealed to a Circuit Court, where a trial *de novo* was had. At such trial the attorney for the bank stated to the court that the bank waived any claim to a preference as to the two thousand-dollar note, but that he could not assent to a judgment to that effect. A judgment was entered sustaining the security for the four thousand-dollar note and avoiding that for the two thousand-dollar note.

The bank subsequently sought to prove that it was a creditor of the estate upon the note for two thousand dollars, and upon two other unsecured notes, aggregating $835.00. The referee refused to allow the proof, upon the ground that, as the bank had compelled the trustee to sue to cancel the security and a judgment nullifying it had been obtained, the bank had lost the right to prove any claim against the estate. The District Judge, upon review, reversed this ruling. The Circuit Court of Appeals to which the issue was taken, after stating the case as above recited, certified questions for our determination.

Mr. Justice White, after making the foregoing statement, delivered the opinion of the Court.

The following are the questions asked by the Court of Appeals:

"First. Can a creditor of a bankrupt, who has received a merely voidable preference, and who has in good faith retained such preference until

deprived thereof by the judgment of a court upon a suit of the trustee, thereafter prove the debt so voidably preferred?

"Second. Upon the issue as to the allowance of the bank's claims was it competent, in explanation of the judgment of the Ohio Circuit Court in favor of the trustee and against the bank in respect to its $2,000.00 mortgage, to show the disclaimer made in open court by the attorney, representing the bank, of any claim of preference, and the grounds upon which the bank declined to consent to a judgment in favor of the trustee?

"Third. If the failure to 'voluntarily' surrender the mortgage given to secure the $2,000.00 note operates to prevent the allowance of that note, does the penalty extend to and require the disallowance of both the other claims?"

Before we develop the legal principles essential to the solution of the first question it is to be observed that the facts stated in the certificate and implied by the question show that the bank acted in good faith when it accepted the mortgage and when it subsequently insisted that the trustee should prove the existence of the facts which, it was charged, vitiated the security. It results that the voidable nature of the transaction alone arose from section 67*e* of the act of 1898, invalidating "conveyances, transfers or encumbrances of his property made by a debtor at any time within four months prior to the filing of the petition against him, and while insolvent, which are held null and void as against the creditors of such debtor by the laws of the State, Territory or District in which such property is situate," and giving the assignee a right to reclaim and recover the property for the creditors of the bankrupt estate.

On the one hand it is insisted that a creditor who has not surrendered a preference until compelled to do so by the decree of a court cannot be allowed to prove any claim against the estate. On the other hand, it is urged that no such penalty is imposed by the bankrupt act, and hence the creditor, on an extinguishment of a preference, by whatever means, may prove his claims. These contentions must be determined by the text, originally considered, of section 57*g* of the bankrupt act, providing that "the claims of creditors who have received preferences shall not be allowed unless such creditors shall surrender their preferences." We say by the text in question, because there is nowhere any prohibition against the proof of a claim by a creditor who has had a preference, where the preference has disappeared as the result of a decree adjudging the preferences to be void, unless that result arises from the provision in question. We say also from the text as originally considered, because, although there are some decisions under the act of 1898 of lower Federal courts, which are referred to in the margin,* denying the right of a creditor to prove his claim, after the surrender of a preference by the compulsion of a

In re Greth, 112 Fed. Rep. 978; *In re Keller*, 109 Id. 126, 127; *In re Owings*, 109 Id. 624.

decree or judgment, such decisions rest not upon an analysis of the text of the act of 1898 alone considered, but upon what were deemed to have been analogous provisions of the act of 1867 and decisions thereunder. We omit, therefore, further reference to these decisions as we shall hereafter come to consider the text of the present act by the light thrown upon it by the act of 1867 and the judicial interpretation which was given to that act.

The text is, that preferred creditors shall not prove their claims unless they surrender their preferences. Let us first consider the meaning of this provision, guided by the cardinal rule which requires that it should, if possible, be given a meaning in accord with the general purpose which the statute was intended to accomplish.

We think it clear that the fundamental purpose of the provision in question was to secure an equality of distribution of the assets of a bankrupt estate. This must be the case, since, if a creditor, having a preference, retained the preference, and at the same time proved his debt and participated in the distribution of the estate, an advantage would be secured not contemplated by the law. Equality of distribution being the purpose intended to be effected by the provision, to interpret it as forbidding a creditor from proving his claim after a surrender of his preference, because such surrender was not voluntary, would frustrate the object of the provision, since it would give the bankrupt estate the benefit of the surrender or cancellation of the preference, and yet deprive the creditor of any right to participate, thus creating an inequality. But it is said, although this be true, as the statute is plain, its terms cannot be disregarded by allowing that to be done which it expressly forbids. This rests upon the assumption that the word surrender necessarily implies only voluntary action, and hence excludes the right to prove where the surrender is the result of a recovery compelled by judgment or decree.

The word surrender, however, does not exclude compelled action, but to the contrary generally implies such action. That this is the primary and commonly accepted meaning of the word is shown by the dictionaries. Thus, the Standard Dictionary defines its meaning as follows: 1. To yield possession of to another upon compulsion or demand, or under pressure of a superior force; give up, especially to an enemy in warfare; as to *surrender* an army or a fort. And in Webster's International Dictionary the word is primarily defined in the same way. The word, of course, also sometimes denotes voluntary action. In the statute, however, it is unqualified, and generic, and hence embraces both meanings. The construction, which would exclude the primary meaning so as to cause the word only to embrace voluntary action would read into the statute a qualification, and this in order to cause the provision to be in conflict with the purpose which it was intended to accomplish, equality among creditors. But the construction would do more. It would exclude the natural meaning of the

word used in the statute in order to create a penalty, although nowhere expressly or even by clear implication found in the statute. This would disregard the elementary rule that a penalty is not to be readily implied, and on the contrary that a person or corporation is not to be subjected to a penalty unless the words of the statute plainly impose it. (*Tiffany* v. *National Bank of Missouri*, 18 Wall. 409, 410.) If it had been contemplated that the word surrender should entail upon every creditor the loss of power to prove his claims if he submitted his right to retain an asserted preference to the courts for decision, such purpose could have found ready expression by qualifying the word surrender so as to plainly convey such meaning. Indeed, the construction which would read in the qualification would not only create a penalty alone by judicial action, but would necessitate judicial legislation in order to define what character and degree of compulsion was essential to prevent the surrender in fact from being a surrender within the meaning of the section.

It is argued, however, that courts of bankruptcy are guided by equitable considerations, and should not permit a creditor who has retained a fraudulent preference until compelled by a court to surrender it, to prove his debt and thus suffer no other loss than the costs of litigation. The fallacy lies in assuming that courts have power to inflict penalties, although the law has not imposed them. Moreover, if the statute be interpreted, as it is insisted it should be, there would be no distinction between honest and fraudulent creditors, and therefore every creditor who in good faith had acquired an advantage which the law did not permit him to retain would be subjected to the forfeiture simply because he had presumed to submit his legal rights to a court for determination. And this accentuates the error in the construction, since the elementary principle is that courts are created to pass upon the rights of parties, and that it is the privilege of the citizen to submit his claims to the judicial tribunals, especially in the absence of malice and when acting with probable cause, without subjecting himself to penalties of an extraordinary character. The violation of this rule, which would arise from the construction, is well illustrated by this case. Here, as we have seen, it is found that the bank acted in good faith without knowledge of the insolvency of its debtor and of wrongful intent on his part, and yet it is asserted that the right to prove its lawful claims against the bankrupt estate was forfeited simply because of the election to put the trustee to proof in a court of the existence of the facts made essential by the law to an invalidation of the preference.

We are of opinion that, originally considered, the surrender clause of the statute was intended simply to prevent a creditor from creating inequality in the distribution of the assets of the estate by retaining a preference and at the same time collecting dividends from the estate by the proof of his claim against it, and consequently that whenever the preference has

been abandoned or yielded up, and thereby the danger of inequality has been prevented, such creditor is entitled to stand on an equal footing with other creditors and prove his claims.

Is the contention well founded that this meaning, which we deduce from the text of the surrender clause of the present act, is so in conflict with the rule generally applied in bankruptcy acts, and is especially so contrary to the act of 1867 and the construction given to it, that such meaning cannot be considered to have been contemplated by Congress in adopting the present act, and hence a contrary interpretation should be applied?

Without attempting to review the English bankruptcy acts or the provisions contained therein concerning what constituted provable debts, and the decisions relating thereto, it is clear that under those acts, where a debt was otherwise provable and the creditor had acquired a lien to which he was not entitled, the English courts in bankruptcy did not imply a forfeiture by refusing to allow proof of the debt because there had not been a voluntary surrender of the preference. On the contrary, where claims were filed against the estate by one who was asserted to have retained a preference, a well-settled practice grew up, enforced from equitable considerations. The practice in question was followed in the case of *Ex parte Dobson*, (4 Deacon & Chitty English Bankruptcy Reports, 69,) decided in 1834, and was thus stated in the opinion of Sir G. Rose (p. 78):

"I apprehend the practice to be settled, where a creditor applies to prove a debt, and claims a right to property to which the commissioners think he has no lien, that the commissioners admit the proof, and leave the question to be controlled merely by retention of the dividend. This was settled by the case of *Ex parte Ackroyd*, [1 Rose, 391,] where the commissioners had rejected the proof of a creditor, because he had received a portion of his debt, which the assignees contended he was bound to refund; but when the question came before Sir *John Leach*, as Vice Chancellor, he decided that the proof of the debt was not to be rejected, because there was a question to be tried between the bankrupt's assignees and the creditor, although it was proper that no dividend should be paid on that proof, until the question was determined."

And Erskine, C. J., p. 78, after assuming that the transaction complained of might have been fraudulent and amounted to an act of bankruptcy, said—italics mine—(p. 75):

"The next part of the prayer is, that the claim should be disallowed. *But though the assignment of the property may be invalid, that will not invalidate the debt of the respondents.* We could not, therefore, disallow the claim, or expunge the proof, if the claim had been converted to a proof; all that we can do is, to restrain the respondents from receiving any dividends, until they give up the property."

Thus the English rule substantially conformed to the construction we have given to the bankruptcy act before us.

Neither our bankrupt act of 1800, (2 Stat. 19,) nor that of 1841, (5 Stat. 439,) contained a surrender clause or any provision generally denying the right of a creditor of a bankrupt to prove his debt in the event that he had received a preference. But, under those acts, bankruptcy courts must necessarily have exercised the power of protecting the estate by preventing a creditor having an otherwise provable debt *who retained* that which belonged to the estate from at the same time taking dividends from it.

The purpose of Congress when a forfeiture or penalty was intended not to leave it to arise from mere construction, but to expressly impose such penalty or forfeiture, is well illustrated by the bankrupt act of 1800, wherein numerous penalties and forfeitures were explicitly declared. Two instances are illustrative. By section 16 it was provided: "That if any person or persons shall fraudulently or collusively claim any debts, or claim or detain any real or personal estate of the bankrupt, every such person shall forfeit double the value thereof, to and for the use of the creditors." And by section 28 it was provided that a creditor suing out a commission, who subsequently accepted a preference, "shall forfeit and lose, as well his or her whole debts, as the whole he or she shall have taken and received, and shall pay back, or deliver up the same, or the full value thereof, to the assignee or assignees who shall be appointed or chosen under such commission, in manner aforesaid, in trust for and to be divided among the other creditors of the said bankrupt, in proportion to their respective debts."

The bankrupt act of 1867, (c. 176, 14 Stat. 528,) contained the following surrender clause:

"SEC. 23. . . . Any person who, after the approval of this act shall have accepted any preference, having reasonable cause to believe that the same was made or given by the debtor, contrary to any provision of this act, shall not prove the debt or claim on account of which the preference was made or given, nor shall he receive any dividend therefrom until he shall first have surrendered to the assignee all property, money, benefit, or advantage received by him under such preference."

And section 35 of the act conferred power upon the assignee to sue to set aside and recover illegal preferences, transfers, etc., but there was not contained in the section any provision prohibiting the proof of claims after recovery by the assignee. In section 39 of the act, however, which was found under the head of involuntary bankruptcy, there was contained an enumeration of the various acts which would constitute acts of bankruptcy, and following a grant of authority to the assignees to sue for and recover property transferred, etc., by the bankrupt contrary to the act, the section concluded with the declaration that when the recipient had reasonable cause to believe that a fraud on the act was intended, and that the debtor was insolvent, "such creditor shall not be allowed to prove his debt in bankruptcy."

Passing the present consideration of the judicial construction given to the act of 1867, and treating, as we believe should be done, the restriction as to the proof of debts expressed in section 39 as applicable to voluntary as well as involuntary bankruptcy, we think, as a matter of original interpretation, the surrender clause of the act of 1867 not only fortifies *but absolutely sustains the construction which we have given to the* surrender clause of the act of 1898. Whilst the surrender clause of the act of 1867 changed the method of procedure prevailing under the English rule, and presumptively also obtaining under the acts of 1800 and 1841, by which a creditor holding a preference might prove his claim but was allowed to obtain no advantage from so doing until he had surrendered his preference, it cannot we think in reason be considered that this mere alteration in the practice to be followed was intended in and of itself to impose a penalty upon a creditor who did not voluntarily surrender his preference. And this we think is demonstrated when it is seen that after making the change as to the procedure in the proof of debts by preferred creditors there was subsequently embodied in section 39 an express prohibition, in the nature of a penalty, forbidding the proof of debt by a creditor who came within the purview of the section. Either that provision solely related to proof of debts embraced in the previous surrender clause or it did not. If it did, then the expression of the penalty in section 39 indicates that it was not deemed that the surrender clause contained provision for the penalty, otherwise section 39 would in that regard be wholly superfluous. If, on the other hand, it be considered that section 39 embraced other debts or claims against the estate than those to which the surrender clause related, then the expression of the penalty in section 39, under the rule of *expressio unius*, could not by implication be read into the previous surrender clause. That is to say, if section 23 and section 39 of the act of 1867 be considered as not in *pari materia*, then it follows that the former, the surrender clause, standing alone, did not impose the penalty or forfeiture provided for in the later. If they were *in pari materia*, then the penalty, whilst applicable and controlling as to both, because of its expression in the later section, cannot be said to have existed alone in and by virtue of an earlier section, wherein no penalty was expressed.

The decisions of the lower Federal courts interpreting the sections in question, as they stood prior to the amendment of section 39 by the act of 1874, hereafter to be referred to, were numerous, and we shall not attempt to review them in detail. They will be found collected in a note contained in the eleventh edition of Bump on Bankruptcy, pp. 550 *et seq.* Disregarding the discord of opinion shown by those decisions concerning what constituted an involuntary surrender—that is, whether it was invol-

untary if made at any time after suit brought by the assignee, or was only so after recovery by the force of a judgment or decree—and putting out of view also the differences of opinion which were engendered by the fact that the forfeiture imposed by section 39 was found in that portion of the act of 1867 which related to involuntary bankruptcy, we think the decisions under the act of 1867, prior to the amendment of 1874, may be classified under four headings.

First. The cases which held that the prohibition of section 39 against the proof of debt operated as a bar to such proof, even although there was a voluntary surrender, where the preference had the characteristics pointed out in section 39. These cases were, however, contrary to the great weight of authority under the act, and the construction which they enforced may be put out of view.

Second. Those cases which, whilst treating the surrender clause as giving a creditor an alternative which he might exercise without risk of penalty or forfeiture, yet held that by the operation of section 39 upon the surrender clause the creditor lost the option to prove his claim, when the surrender was compelled by a judgment or decree at the suit of the assignee. The cases enforcing this interpretation constituted the weight of authority, and such construction may, therefore, be said to have been that generally accepted, and, in our judgment, was the correct one.

These cases, which thus held that the loss of the right to prove, after compulsory surrender, arose not from the surrender clause independently considered, but solely from the operation upon that clause of section 39, are exemplified by the case of *In re Leland*, (7 Ben. 156,) opinion of Blatchford, J. In that case, after holding (p. 162) that the prohibition of section 39 applied as well to cases of voluntary as to cases of involuntary bankruptcy, the court came to consider the surrender clause of section 23 as affected by the penalty provided for in section 39, and said:

"This provision is to be construed in connection, and in harmony, with the provision of the twenty-third section, before cited. If, under the twenty-third section, the preferred creditor were allowed to surrender to the assignee the property received in preference, even after it had been recovered back by the assignee, as mentioned in the thirty-ninth section, so as to be able to prove his debt, no creditor taking a preference would ever be debarred from proving his debt. If, under the thirty-ninth section, it were held that the mere taking of a preference by a creditor would debar him from proving his debt, without the precedent necessity for a recovery back by the assignee of the property conveyed in preference, there never could be any scope for the operation of the twenty-third section in respect to a surrender."

Thus clearly pointing out that by the surrender clause alone the creditor would not be debarred from proving his claim if in fact there had

been a surrender, whether voluntary or not, but that as a result solely of the prohibition of section 39 the creditor would be barred after recovery by the assignee.

Third. Cases which treated the surrender clause as in and of itself forbidding a surrender after recovery, because the recovery authorized by section 35 was the antithesis of the surrender and precluded a surrender after recovery. This class of cases in effect treated the prohibition expressed in section 39 as unnecessary, *quoad* the subject matters to which sections 23 and 35 were addressed. The cases, however, were few in number, and are illustrated by the case of *In re Tonkin*, (4 N. B. R. 52.)

Fourth. Cases which without seemingly considering the incongruity of the reasoning adopted both theories; treated sections 23, 35 and 39 as *in pari materia*, and hence applied the prohibition of section 39 to the other two sections, and yet reasoned to show that the surrender clause alone prohibited a surrender after recovery by the assignee. This class of cases is illustrated by *In re Richter*, (1 Dill. 544, 4 Nat. Bankr. R. 221.) In that case a creditor, who, in consequence of a recovery by the assignee, had surrendered a preference, sought to prove his claim against the estate, and his right to do so was resisted. Analyzing the act and stating the different constructions of which it was susceptible, the court expressly declared that the correct view was to construe sections 23, 35 and 39 together, and that the result of so doing would be to annex to both sections 35 and 23 the penalty provided in section 39. The surrender clause was then noticed, it being said:

"It is urged by the claimants that this refusal was erroneous, because they had, before the time when they made their motion, surrendered to the assignee all property received by them under the preference. This devolves upon us the duty of interpreting the meaning of the word *surrender*, as it is here used. And it is our opinion that a creditor who receives goods by fraudulent preference, and who refuses the demand therefor which the assignee is authorized to make (section 15), denies his liability, allows suit to be commenced by the assignee, defends it, goes to trial, is defeated, and judgment passes against him, which he satisfies on execution cannot be said, within the meaning of the statute, to have surrendered to the assignee the property received by him under such preference. He has surrendered nothing."

As an alternative, however, to this view, and treating the sections referred to as *in pari materia*, it was reiterated that section 23 was limited and controlled by the penalty provided in section 39.

We need not further notice the cases under the act of 1867, because of the action of Congress on the subject. In 1874 (18 Stat. 178) section 39 of the act of 1867 was amended and re-enacted. That amendment consisted of omitting the forfeiture clause as originally contained in the section and substituting in its stead the following proviso:

"*Provided,* . . . and such person, if a creditor, shall not, in case of actual fraud on his part, be allowed to prove for more than a moiety of his debt; and this limitation on the proof of debts shall apply to cases of voluntary as well as involuntary bankruptcy."

Plainly, this amendment not only abolished the penalty provided in section 39 as originally enacted, since it allowed a creditor to prove his claim for the whole amount thereof after recovery against him if he had not been guilty of actual fraud, and even in case of actual fraud after recovery permitted him to prove for a moiety. The amendment clearly also was repugnant to that construction of the act of 1867 given in some of the cases to which we have referred under the third classification, wherein in the reasoning employed it was assumed that a forfeiture or penalty might be implied alone from the terms of the surrender clause, irrespective of the operation of section 39. This results from the very words of the amendment, which says, and this *limitation on the proof of debts* shall apply, etc., showing that the restriction on the right to prove after a compulsory yielding up of a preference was deemed by Congress to result, not from the surrender clause, but from the limitation expressly declared by section 39 as amended, which operated a qualification of the broad terms of the surrender clause. It manifestly also arises from the fact that whilst Congress plainly intended by the amendment to make a change in the rigor of the rule previously obtaining, the phraseology of the surrender clause as originally found in the act was not altered.

After the adoption of the amendment of 1874 it is true that in one or two instances it was held that the amendment, instead of mitigating the severity of section 39 as it stood before the amendment, had increased it by adding an additional limitation, viz., prohibiting a preferred creditor who had been guilty of actual fraud from proving for more than one-half of his claim, even where he had voluntarily surrendered his preference. But these were isolated cases, since practically the otherwise universal construction was that the amendment was remedial and intended by Congress to mitigate, even in cases of actual fraud, the severity of the prohibition of section 39 as originally enacted.

The import of the amendment was tersely stated by Mr. Justice Clifford in *In re Reed*, (3 Fed. Rep. 798, 800,) as follows:

"Beyond doubt the question must depend upon the true construction of the act of Congress, and I am of opinion that Congress intended to moderate the rigor of the prior rules and to allow the creditor, after payment back of the preference, whether by suit or otherwise, to prove their whole debt, in case they had been guilty of no actual fraud."

And such construction was also expounded in the following cases: *In re Currier*, (1875) 2 Lowell, 436; *Burr* v. *Hopkins*, (1875) 6 Biss. 345, per Drummond, J.; *In re Black*, (1878) 17 N. B. R. 399, per Lowell, J.; *In*

re Newcomer, (1878) 18 Ib. 85, per Blodgett, J.; *In re Kaufman*, (1879) 19 Ib. 283, per Nixon, D. J.; *In re Cadwell*, (1883) 17 Fed. Rep. 693, per Coxe, J.

The meaning of the amendment of 1874 was considered by the Court of Appeals of New York in the case of *Jefferson County National Bank* v. *Streeter*, (106 N. Y. 186.) The New York court expressly adopted the construction given in the cases to which reference has just been made, and its action in so doing was affirmed by this court in *Streeter* v. *Jefferson County Bank*, (147 U. S. 40.)

It follows that the construction which we at the outset gave to the text of the act of 1898, instead of being weakened, is absolutely sustained by a consideration of the act of 1867, both before and after the amendment of 1874, and the decisions construing the same, since in the present act, as we have said, there is nowhere found any provision imposing even the modified penalty which was expressed in the amendment of 1874. The contention that because the act of 1898 contains a surrender clause, therefore it must be assumed that Congress intended to inflict the penalty originally imposed by section 39 of the act of 1867 must rest upon the erroneous assumption that that penalty was the result of the surrender clause alone. But this, as we have seen, is a misconception, since from the great weight of judicial authority under the act of 1867, as well as by the express enactment of Congress in the amendment of 1874 and the decisions which construed that amendment, it necessarily results that the penalty enforced under the act of 1867 arose not from the surrender clause standing alone, but solely from the operation upon that clause of the express prohibition contained in section 39 of that act. When, therefore, Congress in adopting the present act omitted to re-enact the provision of the act of 1867, from which alone the penalty or forfeiture arose, it cannot in reason be said that the omission to impose the penalty gives rise to the implication that it was the intention of Congress to re-enact it. In other words, it cannot be declared that a penalty is to be enforced because the statute does not impose it.

And, irrespective of this irresistible implication, a general consideration of the present act persuasively points out the purpose contemplated by Congress in refraining from re-enacting the penalty contained in section 39 of the act of 1867. Undoubtedly the preference clauses of the present act, differing in that respect from the act of 1867, as is well illustrated by the facts of this case, include preferences where the creditor receiving the same acted without knowledge of any wrongful intent on the part of the debtor and in the utmost good faith. (*Pirie* v. *Chicago Title Trust Co.*, 182 U. S. 454.) Having thus broadened the preference clauses so as to make them include acts never before declared by Congress to be illegal, it

may well be presumed that Congress, when it enacted the surrender clause in the present act, could not have contemplated that that clause should be construed as inflicting a penalty upon creditors coming within the scope of the enlarged preference clauses of the act of 1898, thereby entailing an unjust and unprecedented result.

Our conclusion, therefore, is that the first question propounded must be answered in the affirmative, and that the two other questions require no response.

And it is ordered accordingly.

True copy.

Test:

Clerk Supreme Court, U. S.

Supreme Court of the United States.

No. 116.—October Term, 1904.

Guilford B. Keppel, Trustee, etc., vs. Tiffin Savings Bank. } On a certificate from the United States Circuit Court of Appeals for the Sixth Circuit.

[April 3, 1905.]

Mr. Justice Day dissenting.

I am unable to agree with the construction given to the sections of the bankruptcy act under consideration, and because of the importance of the questions involved have deemed proper a statement of the conclusions reached.

Notwithstanding the first question propounded by the Court of Appeals presupposes that the $2,000.00 mortgage was a preference within the meaning of the bankrupt act, it is argued on behalf of the creditors that, although the mortgage made a few days prior to the bankruptcy proceedings and when the bankrupt was insolvent, was void under section 6343 of the Revised Statutes of Ohio, as amended April 26, 1898, (93 Ohio Laws, p. 290,) read in connection with section 67, paragraph *e*, of the bankruptcy act, it did not constitute a preference which must be surrendered, preliminary to proof of the creditor's claim, because there was no actual transfer of any property to the creditor, and the only thing obtained was a void mortgage.

The Ohio statute makes provision, among other things, as to sales, etc., in trust or otherwise, in contemplation of insolvency, or with a design to prefer one or more creditors to the exclusion, in whole or in part, of others, and sets forth:

"And every such sale, conveyance, transfer, mortgage, or assignment made, . . . by any debtor or debtors, in the event of a deed of assignment being filed within ninety (90) days after the giving or doing of such thing or act, shall be conclusively deemed and held to be fraudulent, and shall be held to be void as to the assignee of such debtor or debtors, whereupon proof shown, such debtor or debtors were actually insolvent at the time of giving or doing of such act or thing, whether he or they had knowledge of such insolvency or not. . . ."

By section 67, paragraph *e*, of the bankrupt act, it is provided:

"And all conveyances, transfers, or encumbrances of his property made by a debtor at any time within four months prior to the filing of the petition against him, and while insolvent, which are held null and void as

against the creditors of such debtor by the laws of the State, Territory, or District in which such property is situate, shall be deemed null and void under this act against the creditors of such debtor if he be adjudged a bankrupt, and such property shall pass to the assignee and be by him reclaimed and recovered for the benefit of the creditors of the bankrupt."

Under section 60 of the bankruptcy act of 1898 it was provided:

"*a.* A person shall be deemed to have given a preference if, being insolvent, he has procured or suffered a judgment to be entered against himself in favor of any person, or made a transfer of any of his property, and the effect of the enforcement of such judgment or transfer will enable any one of his creditors to obtain a greater percentage of his debt than any other of such creditors of the same class.

"*b.* If a bankrupt shall have given a preference within four months before the filing of a petition, or after the filing of the petition and before the adjudication, and the person receiving it, or to be benefited thereby, or his agent acting therein, shall have had reasonable cause to believe that it was intended thereby to give a preference, it shall be voidable by the trustee, and he may recover the property or its value from such person."

In section 1, paragraph 25, of the act of 1898, a "transfer" is defined to include the sale and every other and different mode of disposing of or parting with the property or the possession of property, absolutely or conditionally, as a payment, pledge, mortgage, gift or security.

This definition of a transfer covers a mortgage given for the security of a debt in express terms, and section 60 provides that preferences shall include transfers, the effect of the enforcement of which would be to enable any one of the bankrupt's creditors to obtain a greater percentage of his debt than other creditors of the same class.

It is true that if the mortgage is void, it can have no effect to diminish the estate of the bankrupt, but upon its face the mortgage is good as against the bankrupt and the creditors of the estate.

It is said that the mortgage being void, the creditor had nothing to surrender, but this assumes the invalidity of the security. Until set aside or voluntarily surrendered it is a good encumbrance upon the property, whether regarded as a conditional conveyance or as a mere security for the debt. It could be set aside by the trustee upon proof of insolvency of the bankrupt and other conditions named in the act at the time of giving it; otherwise it would stand as a valid security, unless the creditor should elect to surrender it and make proof of his claim as a general creditor.

There seems to be no question that, upon its face, though void in the light of the facts found, this mortgage was one of the transfers of property which was invalidated by the act, it being given within the time limited, and at a time when the bankrupt was in fact insolvent, and expressly made void by the Ohio statute when read with the bankrupt act of 1898.

The answer to the first question requires a consideration of paragraph 57*g* of the act of 1898, which, as it stood prior to the amendment of February 5, 1903, read: "The claims of creditors, who have received preferences shall not be allowed unless such creditors shall surrender their preferences." May a creditor who has received a preference, voidable by the act, contest the validity thereof, and if it is declared invalid, still prove his debt upon surrender of his preference as though no contest had been had?

It was held by this court in *Pirie* v. *Chicago Title & Trust Company*, (182 U. S. 438,) that a creditor who had received a preference, although he did not have reason to believe that one was intended, could only keep the property transferred upon condition of refraining from proof of the balance of his debt.

It was pointed out in that case, in the opinion of the court by Mr. Justice McKenna, that section 60 in its various provisions permitted a creditor, who had innocently received a preference, to hold it if he chose, and it could only be recovered by the trustee in the event that he had reasonable cause to believe that a preference was intended, in which case the trustee might recover the property or its value. But the innocent creditor might keep the property transferred to him, although a preference within the definition of the act, upon terms of non-participation in the bankruptcy estate in the general distribution to the creditors.

Section 23 of the bankruptcy act of 1867 provided: "Any person who, after the approval of this act, shall have accepted any preference, having reasonable cause to believe that the same was made or given by the debtor, contrary to any provision of this act, shall not prove the debt or claim on account of which the preference was made or given, nor shall he receive any dividend therefrom until he shall first have surrendered to the assignee all property, money, benefit or advantage received by him under such preference." Section 57*g* of the present act, prior to the amendment of February 5, 1903, required broadly that claims of creditors who have received preferences shall be surrendered, and that the same shall not be allowed unless this is done.

Under the former act the surrender was required of creditors who had accepted preferences, having reasonable cause to believe the same contrary to the provisions of the act, and such creditor could not receive any dividend until he had first surrendered the preference. In passing the act of 1898, Congress doubtless had before it prior legislation on the subject, and particularly the act of 1867, the most recent enactment on the subject.

Section 57*g* provides that all preferences, whether innocent or otherwise, shall be surrendered before the creditor can prove his claim, and the right of proof is not postponed *until* the surrender, but claims are not to be allowed *unless* creditors shall surrender their preferences. The element of time is indicated in the word "until," which means to the time of, or up to,

while the use of "unless" more emphatically denies the right of proving the claim, save or except upon terms of relinquishing the preference.

In view of the purpose of the bankruptcy act to make an equal distribution of the bankrupt's estate among creditors of the same class and to avoid preferences made within four months, I think, having in view the first question put by the Circuit Court of Appeals, that the sections of the law in question must be construed to put a creditor who has received a merely voidable preference, which could be recovered from him by the trustee, to his election betweeen striving to retain that which he has received, and voluntarily surrendering his preference, and filing his claim that he may participate with other unsecured creditors in the general distribution of the estate.

The law looks to a prompt, equal and inexpensive distribution of the estate among those entitled thereto, and I do not think it was intended to permit a creditor to take the chances of litigation with the trustee, and when defeated still have the right to "surrender" his preference and participate in the distribution of the general estate. I think the surrender contemplated by the law is not the capitulation which comes after unsuccessful resistance, but is intended to require the creditor, who must be presumed to know the law, to make a prompt election and to stand or fall upon the choice made. In other words, it was not intended to permit a creditor who holds security liable to defeat under the law to keep it if he can maintain it by successful contest and, if not, to have the same right and privilege as to proof of his debt that he would have if he promptly availed himself of the privilege of surrender which the law gives to one who would place himself upon a general equality with other creditors of the estate.

These conclusions are sustained by a consideration of the terms of the law under discussion, as well as the adjudicated cases which have arisen under it. The act of 1898 made important changes when compared with the bankrupt law of 1867. As we have already seen, section 23 of the latter act limited the requirement as to the surrender of preferences to those made or given contrary to the provisions of the act. Section 35 of the same law gave the right to the assignee in bankruptcy to set aside illegal preferences, and section 39, after enumerating certain transactions which should amount to acts of bankruptcy, including fraudulent conveyances as therein described, provided that whenever the beneficiary had reasonable cause to believe that a fraud upon the act was intended, or the debtor was insolvent, the assignee might recover the property, and the creditor should not be allowed to prove his debt in bankruptcy. In 1874, (18 Stat. 178,) section 39 of the act was amended, and, instead of prohibiting a creditor who had received a conveyance in fraud of the act from proving his debt, it was provided that such creditor should not, in

case of actual fraud on his part, be allowed to prove for more than a moiety of his debt, and this limitation should apply to cases of voluntary as well as involuntary bankruptcy.

It will not, in my view, aid in the determination of the proper construction of the act of 1898 to review the numerous and conflicting decisions made under the act of 1867 as to the effect of these various provisions upon the right of the creditor to prove his claim. The great weight of authority is that one who had a voidable preference under the act could not be permitted to prove his claim after a judgment had been rendered against him in a contest with the trustee.

Presumably with the provisions of the act of 1867 before it, providing that in certain cases of fraudulent conveyance the creditor could not prove his claim in bankruptcy, first as to the whole, and later as to a half of the debt, and the limitations of the requirement to surrender preferences to those made in violation of the act, Congress laid aside these requirements, and broadly provided in section 57*g* of the act of 1898 that all preferences must be surrendered as a condition of proof of claims against the estate The innocent holder of a preference could not be deprived of his right of election between proof of his debt and the surrender of his preference. He who had a voidable preference might surrender it and prove his debt. If he did not "surrender," the trustee could recover the preference, and the privilege of proof which was conditioned upon surrender no longer existed.

Prior to the amendment of 1903 this court, in the case of *Pirie* v. *Trust Company*, already referred to, decided that the requirement extended to all manner of preferences, whether innocently received or otherwise, and this was the law until the amendment of 1903.

Therefore the sole question here is: What is meant by the term "surrender" as used in the act of 1898?

We have been referred to four cases decided under this law before the passage of the amendment of 1903. Before passing to them I may refer to a decision of Judge Dillon at the circuit, (*In re Richter*, 1 Dill. 544,) rendered in 1870 under the act of 1867, but in defining the word "surrender," and pointing out its meaning, the language of the learned judge is as pertinent now as it was then. Having before him the construction of the term "surrender" as used in section 23 of the act of 1867, and speaking of the right of a creditor to prove the balance of a claim which had been illegally preferred, the judge said:

"The statute is that they shall not prove up the debt or claim on account of which the preference was given. It was this precisely which, by the motion under consideration, they sought to have done, and which the court refused to allow.

"It is urged by the claimants that this refusal was erroneous because they had, before the time when they made theirmotion, surrendered to the

assignee all property received by them under the preference. This devolves upon us the duty of interpreting the meaning of the word *surrender*, as it is here used. And it is our opinion that a creditor who receives goods by way of fraudulent preference, and refuses the demand therefor which the assignee is authorized to make (section 15,) denies his liability, allows suit to be commenced by the assignee, defends it, goes to trial, is defeated and judgment passes against him, which he satisfies on execution, cannot be said, within the meaning of the statute, to have surrendered to the assignee the property received by him under such preference.

"He has surrendered nothing. He accepted a fraudulent preference and defended it to the last. Paying a judgment which he stoutly resisted, and from which he could not escape, is not such a surrender as the statute contemplates. To hold that it was would be against the spirit of the statute, which is to discourage preferences. Such a holding would manifestly encourage them, for if the transaction should be upheld the creditor would profit; if overthrown, he would lose nothing, and stand upon an equal footing with those over whom he had attempted to secure an illegal advantage, and whom he has, by litigation, delayed in the collection of their claims."

The question, under the act of 1898, came before the United States District Court for the Northern District of Iowa, in the case of *In re Keller*, (109 Fed. Rep. 118, 6 Am. B. R. 334,) where the subject is discussed by Judge Shiras. Summing up the matter, the learned judge said:

"It would certainly be wholly inequitable to hold that a creditor who has received a preference from an insolvent debtor can refuse to account therefor, and after causing the other creditors the delay, cost, and expense of litigation, after being defeated therein, can still prove up his claim, and take an equal share in the proceeds of the estate after depleting the same in the manner stated. Contesting the claim of the trustee, and paying back the preference in obedience to the process of the court, is not a surrender, within the meaning of clause '*g*' of section 57. Therefore there is this difference between a preferred creditor who surrenders a preference and a preferred creditor from whom the preference is recovered by the trustees; the former, having voluntarily surrendered the preference received, is entitled to prove up his entire claim, and share with the other creditors. The latter, having refused to surrender, cannot prove the claim or share in the estate."

To the same effect is *In re Owings*, (109 Fed. Rep. 623,) and in *In re Greth*, (112 Fed. Rep. 978, 7 Am. B. R. 598,) the cases are reviewed and the same conclusion reached.

In Collier on Bankruptcy, third edition, section 319, that author says:

"The question what constitutes a surrender has received much discussion. It is admitted by all that if the assignee is compelled to bring an action to invalidate a transfer, and if he recovers and enters up a judgment, no subsequent payment of that judgment by the preferred creditor

and no subsequent compliance by him with its terms can be considered a surrender. By his judgment the trustee has 'recovered' the property. In legal effect the transferee no longer has anything to surrender."

And in the fifth edition of the same work, p. 420, it is said:

"What is a surrender.—Here the doctrines declared under the law of 1867 seem at least somewhat applicable. The phrasing of that statute undoubtedly colored some of the decisions under it. But, under well-recognized principles of law, a surrender that is compulsory is not a surrender. The element of fraud is usually present, but may be lacking; the test is: was the act a voluntary one? Each case turns on its own facts and there is some conflict, but the weight of decision under the present law supports this view."

The only case, decided under the act of 1898, which has come to my attention sustaining a contrary view is *In re Gerson Richard*, (94 Fed. Rep. 633, 2 Am. B. R. 506,) in which it was decided that, notwithstanding the preference was set aside, after a fruitless fight with the trustee, the creditor might prove his claim.

We are cited to *Streeter* v. *Jefferson National Bank*, (147 U. S. 36,) as sustaining the contrary view of the meaning of the term "surrender" as used in this act. The case was under the act of 1867. But in that case the contest was over a stock of goods, and the creditor, the bank, had consented through its attorneys to the appointment of a special receiver, who was ordered to sell the goods and pay the proceeds into court. Of this feature of the case Mr. Justice Shiras, who delivered the opinion of the court, said (p. 45):

"To sustain the contention that the bank did not surrender its preference, it is urged that the bank did not at once, on demand of the assignee, turn over the goods levied on, but litigated the matter with the assignee in both the District and the Circuit Courts, and that the proceeds of the execution were not relinquished until final judgment was entered against the bank.

"It was the opinion of the State court that, as the sheriff, having custody of the goods seized on execution, was, with the consent of the bank's attorneys, appointed special receiver, and was ordered to sell the goods and pay the proceeds into court, to await the result of the litigation between the bank and the assignee in bankruptcy, and that as the proceeds were finally turned over to the assignee, and thus became subject to distribution as bankruptcy assets, the transaction amounted to a surrender under section 5084. In so holding we think the State court was right."

We are also cited to the meaning of the word "surrender" as given in the Standard Dictionary:

"1. To yield possession of to another upon compulsion or demand, or under pressure of a superior force; give up, especially to an enemy in warfare; as to *surrender* an army or a fort."

This definition is given in support of the contention that a surrender may sometimes be made involuntarily. This is doubtless true, and ob-

viously the term may have different meanings when used in different connections. It may be that an army may surrender a fort after a most vigorous contest, while there is still the choice between further resistance and yielding the fortress to an enemy, but the most liberal meaning of the term could hardly describe as a surrender the occupation which a victorious army has gained of a fort after it has ejected the enemy from its walls and is securely intrenched therein without leave of those who have been forcibly driven out.

The bankrupt law contemplates that a secured creditor, who holds a security voidable under the law and which he should put into the common fund as a condition of the right to participate with other unsecured creditors in the division of the estate, must make his choice while he has yet something to give for the privilege of being taken from the class of those who have a security which may be taken from them, and placed in a class, always favored in the bankrupt law, who shall share in the equal distribution of the bankrupt's estate, freed from fraudulent conveyances and voidable preferences.

The complete answer to the argument that one who has received a preference which he must give up before proof as a general creditor has the right to try out with the trustee the question of the validity of the preference and then surrender, is that when the judgment of the law has taken the preference from him he has nothing left to surrender, and if then so disposed the creditor cannot surrender a thing which has been wrested from him by the strong hand of the law.

In this case the Ohio statutes, when read with the bankrupt law, distinctly avoid preferences, and the trustee, by bringing the action, diminished the estate and delayed its distribution. The creditor, before the litigation, had his election as to the course he would pursue. While he had something to surrender he might give it up, prevent costs, delay and litigation, and aid the speedy and equal distribution of the bankrupt's estate. After two judgments against him, and when he had absolutely nothing to give up to the bankrupt's estate, it is, in our view, too late to "surrender."

I think the construction here given comports with the purposes and carries into effect the design of the act as expressed by its terms. It is true that in the present case, after resisting the attack upon the $2,000.00 mortgage in the Court of Common Pleas, and when the judgment had gone against the bank it did not appeal, and its counsel in the Circuit Court disclaimed intention to insist upon the preference of the $2,000.00 mortgage, but even then refused consent to a decree against the mortgage, and in our opinion the time of election was before judgment in the court of original jurisdiction wherein the mortgage was contested and defeated. It is unnecessary to consider whether an election to surrender the preference can be made after

issue joined and before judgment. In this case a trial was had upon the merits. The judgment rendered was vacated by the appeal and in the appellate court, notwithstanding the qualified disclaimer of counsel for the bank, a final judgment was rendered against the mortgage.

These considerations lead to the conclusion that the first and second questions should be answered in the negative.

The importance of the ruling just made is shown in its application not only to the act of 1898 as it originally stood, but to the act as it now stands since the amendment of February 5, 1903, which only requires a surrender of preferences when the same are in violation of subdivision *b* of section 60, or void or voidable under § 67, subdivision *e*. The reasoning of the majority of the court permits the holder of a preference, no matter how fraudulent, to contest with the trustee when his preference is attacked, and when convicted of fraud and an intention to defeat the purposes of the law to "surrender" that which the law has declared he cannot hold, and prove his debt as a general creditor. To permit this seems to me to defeat the purpose of the act and to encourage the very thing the surrender clause was intended to promote—a prompt and inexpensive distribution of the estate. The fraudulent transferee, although he has lost his suit, has taken no risk, and may still prove his claim on an equality with unpreferred creditors over whom he has sought an illegal advantage. I cannot agree with this construction, and therefore dissent from the judgment and reasoning of the majority of the court.

I am permitted to state that Mr. Justice HARLAN, Mr. Justice BREWER, and Mr. Justice BROWN concur in this dissent.

True copy.

Test:

Clerk Supreme Court, U. S.